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TAGS: EFIN EAID ECON NP GON
SUBJECT: NEPAL'S FY 03 BUDGET FOCUSES ON SECURITY, CUTS DEVELOPMENT EXPENDITURE

SUMMARY

¶1. (SBU) On July 8 Prime Minister Sher Bahadur Deuba presented a budget that for the first time puts "maintaining peace and security" in the face of the Maoist insurgency ahead of poverty alleviation as an "overriding priority." Introduced by royal ordinance in the absence of Parliament, the FY 03 budget increases security-related expenditures by 43 percent while cutting development expenditures by 23 percent. The lean budget, which features the narrowest margin of increased expenditures ever, comes in the context of a dismal .8 percent growth in GDP. End summary.

BUDGET BY ORDINANCE

¶2. (U) On July 8 Prime Minister Sher Bahadur Deuba presented the USD 1.2 billion FY 03 budget to an assembly that included dignitaries from the Government of Nepal (GON), representatives from the undissolved Upper House of Parliament, and members of the diplomatic community at the National Planning Commission. The PM prefaced his speech by justifying both his decision to extend the state of emergency and his move to dissolve the Lower House of Parliament. In the absence of Parliament, the budget had been approved by royal ordinance earlier the same day. Nepal's fiscal year begins July 17.

¶3. (U) The budget, presented in the shadow of the six-year-old Maoist insurgency, an extended state of emergency, a dissolved Lower House of Parliament, and impending national elections, was remarkable for several "firsts." Projected expenditures, for example, for the first time declined (albeit by a modest 3 percent) in comparison to the previous fiscal year. Another first: "maintaining peace and security" displaced poverty alleviation as an "overriding priority" for the first time. Thus requested levels for regular expenditures (about USD 736.4 million), boosted by a 43 percent surge in defense spending, outstripped requests for development expenditures (about USD 495.8 million). An effort to aim at more realistic revenue estimates, based primarily on improved tax and customs collection and increases in import duties for certain goods, resulted in projections 9 percent lower than the previous year. Revenues are expected to account for about 58 percent of expenditures, with foreign grants and loans making up an additional 15 percent and internal and external borrowing another 12.5 percent. A budget deficit that is 5.2 percent of GDP is projected.

WHAT MADE THE CUT

¶4. (SBU) Since "development is not possible without peace," funding for the Ministries of Home and Defense together accounted for the single largest percent (23.6 percent) of regular expenditures. Regular expenditures in general will be trimmed by an embargo on the procurement of new vehicles (except for the security forces), contracting out of cleaning and guard services for government offices, and the elimination of redundant positions in the Public Service Commission and in loss-making state-owned enterprises. The PM ranked poverty alleviation and employment promotion next after this "investment for peace" required by the security forces. Electricity and road construction programs received the most generous allotment of development expenditures at 18 and 10 percent respectively, while education, irrigation, and health services netted 8.5 percent, 7.7 percent, and 7.1 percent respectively.

¶5. (SBU) Some of the development projects that escaped elimination under the uncharacteristically austere budget included improved credit programs for agricultural borrowers; subsidized training programs for former Maoists; micro-hydropower schemes to provide electricity to another

5,000 households; the repair of infrastructure damaged by the insurgents; expanded Food for Work programs for former bonded laborers; and agricultural extension programs for apiculture, sericulture, and livestock raising for remote rural areas. The budget provided funding in the amount of approximately USD 7 million for national elections, now scheduled for November 13. In an acknowledgement of widening unemployment figures, the PM also announced the Government plans to send 100,000 young people abroad for foreign employment, with priority given to "people from poor, downtrodden and ethnic groups." Foreign investment will be promoted by offering ten-year, multiple-entry visas to non-resident Nepali investors and by creating "a congenial atmosphere" for investors of other nationalities. Funding to begin construction of an Export Processing Zone in the border city of Bhairawa is also set aside.

GRIM GROWTH FIGURES

¶6. (U) The budget presentation followed closely upon the release of the annual Economic Survey, which reported a mere .8 percent in GDP growth in FY 02, the smallest increase in 18 years. (Note: FY 01 GDP growth was 4.7 percent, while 6.14 percent growth was posted in FY 00. End note.) Agricultural productivity grew by only 1.7 percent, compared with 4.3 percent the previous year. Non-agricultural growth, dragged down by the struggling tourism and garment industries, meanwhile, grew by a minute .2 percent, compared with 5 percent the previous year. Per capita income declined from USD 240 to USD 226 during FY 02.

¶7. (SBU) The depressing performance of the current year notwithstanding, the Government of Nepal (GON) is nonetheless predicting an optimistic aggregate economic growth rate of 4.3 percent during the upcoming fiscal year. Much of the anticipated increase is predicated upon an inexplicably projected 4.9 percent increase in the non-agricultural sector.

COMMENT

¶8. (SBU) So far the FY 03 budget has generated only muted static from some quarters, including the Opposition Communist Party of Nepal - United Marxist Leninist (UML), both for its slicing of the usual array of development programs and its introduction despite the dissolution of Parliament. While its estimates for next year's growth seem somewhat rosier than warranted--especially since we see no immediate relief in sight for the depressed garment and tourism industries--the GON appears to have made a legitimate effort to meet donor demands to pare expenditures and develop more modest projections for revenues. In prior years the GON had proved unable to spend all of the funds allocated for development; the soaring costs of the insurgency have now forced it to prioritize its spending. The scuttling of many GON-funded development projects is an unfortunate, but inescapable, casualty of the insurgency.
MALINOWSKI